

ACHIEVE *Issue Brief*

June 2000

STATE OF CONNECTICUT

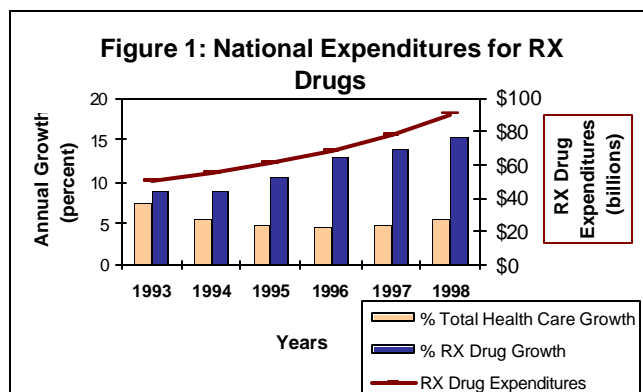
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OFFICE OF HEALTH CARE ACCESS

The rising cost of prescription medication has become an important issue in health care financing. Managing the steady increase in prescription drug costs continues to pose a challenge to policy makers, consumers, insurers and employers alike. This policy brief provides a general overview of the current debate over rising prescription drug costs. Subsequent briefs will provide additional information on this issue.

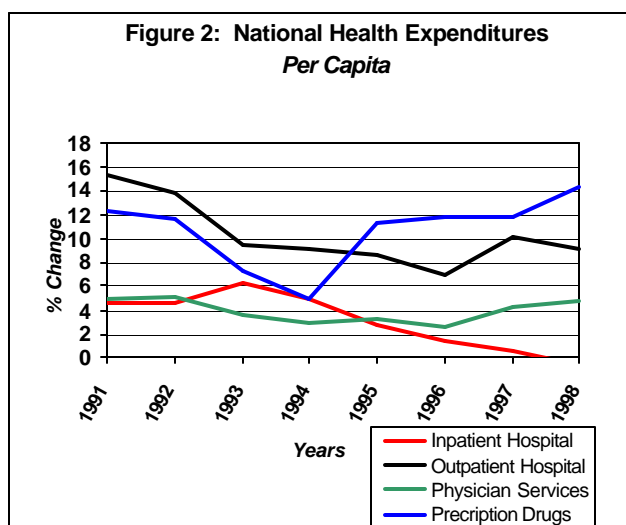
National Trends in Pharmaceutical Expenditures

National pharmaceutical expenditures increased from \$50.6 billion in 1993 to about \$90.0 billion in 1998.¹ This figure is estimated to reach \$105 billion in 1999 and to more than double to \$212 billion by 2004.²



General Accounting Office Testimony, *Prescription Drugs*, HCFA, Office of the Actuary, February 16, 2000.

While the benefits of new prescription drugs are irrefutable, their increased costs have a major impact on total health care spending. Recent trends show that when taken as a share of overall health care spending, pharmaceutical expenditures have seen a sharp increase while spending in other areas has declined. The dramatic differences between these expenditures become evident when comparing the cost trends of prescription drugs against those of inpatient hospital services. From 1991 to 1998, per capita spending on prescription drugs grew while the percentage of spending on inpatient hospital service decreased significantly (*Figure 2*).



States Face Increased Expenditures for Pharmaceuticals, National Governors' Association & NGA Center for Best Practices, February 3, 2000 (data from Milliman & Robertson Health Cost Index, expanded to include Medicare).

Why have prescription drug costs risen so dramatically?

Several factors have been identified as the major drivers of increased prescription drug cost:

- Increased costs of research and development initiatives for new prescription drugs
- Increased prescription drug usage, *especially* among a rapidly growing aged population
- Lack of monitoring of drug usage resulting in possible duplication and misuse
- FDA changes in 1985 and 1997 of direct-to-consumer drug advertising laws, creating greater consumer demand^{3 4}
- Increased utilization resulting from more generous prescription drug benefits (offered through managed care)

The notion that research and development efforts are major drivers of increasing costs has been widely debated.

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Some drug companies contend that the expense of developing new drugs is reflected in higher prices and that price controls would only impede progress; others believe that research and development expenses are not new to the industry and therefore cannot account for such dramatic cost increases.⁵ More research must be done to determine the extent to which independent factors contribute to this growing trend.

Is the trend of rising costs likely to continue?

Because use among an aging population is expected to further increase the demand for prescription medications, this trend is expected to continue. Additionally, a significant increase in the number of newer, more expensive drugs released on the market will contribute to this rising trend. Less expensive, generic substitutes become available only after the patent period for new drugs runs out. This further limits options of less expensive alternatives. The lack of equally effective, lower cost substitutes has a profound economic impact on fixed-income seniors.

Future Discussion

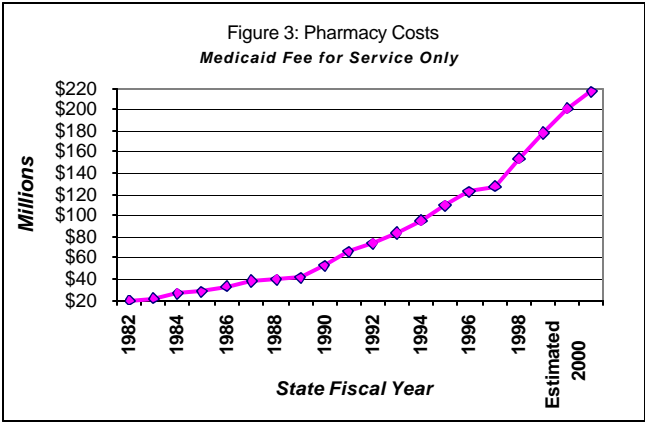
Fueling the debate over rising drug costs are allegations that pharmaceutical companies engage in unfair pricing practices. Calls to impose drug-pricing controls have been heard from both state and federal regulators. At first glance, a policy limiting the amount a drug manufacturer is allowed to charge for specific prescription drugs may appear an effective approach to managing costs, but the long-term economic impact of such a policy is difficult to project.

As the purchaser of health care services for its state employees, retirees and Medicaid population, Connecticut is faced with the difficult task of developing

strategies to manage prescription drug costs. For example, pharmacy costs incurred by Connecticut’s Medicaid fee-for-service population jumped from \$84 million in 1993 to \$154 million by 1998. This cost is expected to reach \$201 million in 2000 (*Figure 3*).

A primary goal of the *ACHIEVE* initiative is to leverage the state’s purchasing power to effectively manage health care costs. Managing and controlling pharmaceutical costs will be a key component of any strategy the state implements. Connecticut, like other health care purchasers, will continue to face budgetary pressures to meet expected pharmaceutical spending increases. Some of the policy options available to purchasers include: instituting “collaborative practices” between physicians and pharmacists, restricting and modifying formularies, and shifting more costs to the consumer in the form of tiered co-payment structures. Policy options discussed by other states have included expanding state prescription drug assistance programs (which serve elderly and disabled populations) and developing prescription drug management programs to monitor drug use and avoid costly duplication.

As the issue of rising drug costs continues to be explored, policy makers at the state and federal level will be called upon to balance the significant cost of prescription drug expenditures with other, equally important budgetary demands. Additional study will be needed to identify the drivers of cost increases and better inform participants in future debate on this issue. Future issue briefs will augment this policy discussion with Connecticut-specific information where possible.



State of Connecticut Office of Policy and Management, *Medicaid Fee for Service Pharmacy Costs*

This information is presented by OHCA to inform policy makers, the public and the health care industry. For further details, please call (860) 418-7028.

¹ Health Care Financing Administration, *National Health Expenditures by Type and Expenditure*, January 1, 2000.

² *Drug Cost Debate Continues, but Drug Industry Eschews Price Controls*, Health Care Policy 2000, Bureau of National Affairs, Vol. 8, No. 19, pp.749-753.

³ Matthew F. Hollon, MD, *Direct to Consumer Marketing of Prescription Drugs*, Journal of the American Medical Association, Vol. 281, No.4, January 27, 1999, pp. 382-389.

⁴ *FDA to Review Standards for All DTC RX Drug Promotion*, U.S. Department of Health and Human Services News, August 8, 1997.

⁵ *Drug Cost Debate Continues, but Drug Industry Eschews Price Controls*, Health Care Policy 2000, Bureau of National Affairs, Vol. 8, No. 19, pp.749-753.